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Supreme Court of the United States

October Term, 1939.

No. 719.

THE COLORADO NATIONAL BANK OF DENVER,
a National Banking Association,
Appellant,

vs.

HOMER F. BEDFORD, as Treasurer of the State of Colorado,
Appellee.

APPEAL FROM THE SUPREME COURT OF THE STATE OF COLORADO.

REPLY BRIEF OF APPELLANT.

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INTRODUCTORY STATEMENT.

In this reply to appellee's brief, it is not our purpose to repeat any of the arguments made in our opening brief filed herein, nor to reply, in detail, to all of appellee's contentions or to all of his citations. We consider many of his points sufficiently answered, and many of his citations

sufficiently explained, in our opening brief, or as needing neither answer nor explanation. We intend to avoid both repetition and needless argument. Consequently, our silence upon any subject is not a concession on our part of the correctness of the position taken by appellee upon it. His principal contentions, which we believe may merit or require reply, are indicated in the headings which follow, though we have not arranged them in the order in which he advances them nor used the exact words of his headings.

All italics in this brief are ours.

1. *Reply to argument that constitutional questions were not properly preserved and are not involved.*

Permeating appellee's entire brief is his argument that the constitutional questions upon which we rely were not properly raised in the court below, and so may not now be considered in this court. His specific statement in this respect is made toward the end of his brief, which we quote with our own insertions of parenthetical numbers, as follows:

> "We must here again point out the fact that these contentions are not in the pleadings, or properly before either the Supreme Court of Colorado or this Honorable Court on Appeal. Appellant is bound by its answer filed in the original case. (1) That answer contains no allegation that the Public Revenue Service Tax Act is contrary to the Constitution of the United States or the laws of the State of Colorado; except that the bank is immune by virtue of its being a federal agent. (2) The findings of law entered by the trial court fail to cover these contentions. (3) They were not included in the bill of exceptions and assignments of error filed with the Supreme Court of Colorado in the case of Bedford, Treasurer, v. Bank, the subject matter of this appeal." (Appellee's Brief, pages 28-29.)

The foregoing is wholly erroneous—probably due to oversight arising through the appellee's representation in this court and in the state courts by different assistant attorneys general. The errors are easily demonstrated.

As to proposition numbered (1) above, contrary to the statement therein made, the bank's answer alleged the following:

> "8. That the subject of this action and the matter in controversy is a suit of a civil nature, in equity, and arises under the Constitution or laws of the United States, or both.
>
> 9. That the said controversy arises because of the plaintiff's said rulings, regulations or interpretations of the said Service Tax Act and the Bank's contentions that they are invalid, unlawful, unconstitutional and improper as applied to the Bank; and that its said contentions are as follows, to-wit:
>
> (1) That the said Service Tax Act expressly provides in part, in recognition of the Constitution of the United States and of the Acts of Congress, restricting taxation of national banks, that 'all services rendered or performed which the State of Colorado is prohibited from taxing under the Constitution or laws of the United States shall be exempt from taxation,' under the said Act; that the depository service of the Bank is part of its banking business under its federal charter and within the said quoted exemption; *and that the said quoted provision should be construed and interpreted as exempting the Bank's said service from taxation because it would otherwise be subjected to the other provisions of the said Act, which must then be held unlawful and unconstitutional as against it and which are as follows, to-wit:*"

(R. 8, and then follow specifications (a) to (g), inclusive, pleading, in detail, the various methods in which the Service Tax Act violates the bank's federal rights unless the bank's services are exempt.)

And the answer then proceeds:

> "(2) That the Bank, as a national bank, is a governmental agency or instrumentality of the United States; that the defendant in enforcing, or attempting to enforce, the said Service Tax Act as to the Bank, as hereinbefore alleged, is imposing a tax against the Bank in contravention of the constitutional immunity of the United States and their governmental agencies and instrumentalities, and under color of the said Service Tax Act and under color of his rulings, regulations or interpretations with respect thereto is seeking to deprive the Bank of a right, privilege or immunity secured to it by the Constitution of the United States." (R. 10.)

Note that by these allegations, the bank contended and alleged, in the alternative, that the state law, if properly construed, exempted its services from taxation, and that, if otherwise construed and applied, it would violate the United States laws and Constitution. In so doing, the bank followed a course approved in *First National Bank v. Anderson*, 269 U. S. 341, 345; 46 S. Ct. 135, 137—a case which appellee cites and quotes.

As to these allegations and contentions, the trial court, in its first judgment and decree (contrary to appellee's statement numbered (2) that it failed to "cover" them), found and determined:

> "That the defendant is a national banking association, organized and existing under and by virtue of the Constitution and the Acts of Congress of the United States of America, and as such is an agency or instrumentality of the United States; that the

services performed by the defendant in operating safety deposit boxes and vaults are incident to and an integral part of, its banking business, for the performance of which it was and is chartered and enfranchised as such governmental agency or instrumentality; that as to any service tax imposed upon the said services under the Colorado Public Revenue Service Tax Act of 1937, the defendant Bank as the one rendering or performing such services *would be the taxpayer, or, if not, would be burdened by such a tax;* and that, therefore, the said services are by Section 7 of the said Act expressly exempt from taxation under it as 'services rendered or performed which the State of Colorado is prohibited from taxing under the Constitution or laws of the United States or the State of Colorado.'" (R. 16.)

And it decreed:

"1. That all services performed by defendant in operating safety deposit boxes and vaults are exempt from taxation under the said service tax law of Colorado." (R. 17.)

Appellee's next statement, numbered (3), that the bank did not include these matters in a bill of exceptions or in assignments of error in the Colorado Supreme Court in the case of *Bedford, Treasurer, v. the Bank* (R. 19), indicates to us some misunderstanding. That case (see R. 19, et seq.) was the first cause on error; *prosecuted by the Treasurer to seek a reversal of the district court's said decision in favor of the bank.* The bank had no reason to include, and in fact could not include, either a bill of exceptions or assignments of error, in the Treasurer's review of a decision of the district court in which the bank was successful.

It was not until the Colorado Supreme Court had held, in reviewing the first judgment and decree, that the bank's

services were *not* exempt, and the district court, upon remand, was about to enter its second judgment and decree, that the bank could do anything further to preserve its rights under the United States Constitution and laws, with respect to the burdens then and for the first time cast upon it.

That it then did so is shown by its bill of exceptions (R. 31-34), in which it made its objections and exceptions specifying, in detail, and specifically naming Art. I, Sec. 8; Art. II, Sec. 10; Art. V of Amendments; Art. XIII, Sec. 1, of Amendments; and Art. XIV, Sec. 1, of Amendments, of the United States Constitution (see R. 32-34).

These same grounds were assigned as error in the Colorado Supreme Court in the cause on error, prosecuted by the bank (see R. 38-41), and are assigned as error in this court (see R. 43-46).

That these federal questions were inherent and presented in this litigation at its inception is shown also by the Treasurer's own allegation (admitted in the answer) made in his verified petition:

> "The nature of such controversy (meaning the controversy between him and the bank to be decided in the litigation), in substance, is that the act in naming banks as rendering a taxable service was, in effect, *imposing a tax upon banks in conflict with federal law and hence, invalid as to banks:*" (Par. VIII, R. 4.)

All of the foregoing, it seems, have been overlooked or forgotten. Overlooked or forgotten also is the position taken by the Treasurer in the Colorado Supreme Court as to the involvement of United States constitutional questions. When that court at first affirmed the first judgment

and decree of the district court (R. 18), the Treasurer in his petition for a rehearing filed in that court, which was granted (R. 19), said:

> "The primary purpose of this action was to obtain a judicial interpretation of the meaning of certain provisions in the Public Revenue Service Tax Act of 1937. Specifically, the interpretation sought was, whether or not the burden of the tax imposed by the act is upon the one performing the service or upon the consumer or user of the service, *and whether or not the duty of collecting such service tax imposes upon an agency of the United States Government an unconstitutional burden.* The equally divided opinion of this court, without written opinion, leaves us without any clear and adequate judicial interpretation of the questions raised.
>
> • • • • • •
>
> If the service tax is judicially held to be imposed upon the consumer or user of the service, as above indicated, then the other sole remaining question would be whether or not the duty of collecting and remitting the tax would be an unconstitutional burden upon the national bank. *Such a question would be one subject to review by the United States Supreme Court, and for such purposes a clear and concise opinion of this court should be given.*"

Furthermore, it clearly and unmistakably appears from the Colorado Supreme Court's opinion (R. 19) that it actually considered these federal questions and decided against the claims of federal right, and the decision of the question was essential to the judgment rendered. (*Chambers v. Baltimore*, 207 U. S. 142, 28 S. Ct. 34.)

As we view the case, no record could be stronger in warranting exercise of jurisdiction by this court. Neither

the record nor any of appellee's cited cases defeat it. We discuss but a few of them under the heading

2. *Reply to argument that state court's decision was of a local question and is binding on this court.*

We understand appellee's theory to be that, because the state supreme court held, as he believes, that the bank, as the performer of services is not the taxpayer, this court may not inquire into the matter, though the state supreme court also held, affirming the district court's second judgment and decree, that the bank must pay the tax, *whether collected or not from the user of its services.*

He relies upon *Farncomb v. Denver*, 252 U. S. 7, 40 S. Ct. 271, which dealt with the validity of a charter provision of the City of Denver relating to local improvement assessments, previously construed by the Colorado Supreme Court, and as so construed held valid in *Londoner v. Denver*, 210 U. S. 373, 28 S. Ct. 708. He also relies upon *Alvard v. Johnson*, 282 U. S. 509, 51 S. Ct. 273. It appears from this cited case that the tax was a "property" tax—a tax upon the plaintiff's tangible property, measured by his income from its use. It was a tax, *in lieu of all other taxes*, levied state-wide against the property of all persons engaged, as the plaintiff was, in using the state's roads, rights of way, etc. It was not in any respect a tax upon the plaintiff's franchise, occupation or business.

In the cause at bar, however, the tax in question must be considered as a *tax upon the bank's safe-deposit business.* It cannot be considered a *property* tax upon the bank's vaults and safe-deposit boxes, measured by its income therefrom, because the Treasurer, by his demurrer, has admitted the allegations of the bank's answer that the state has *elected (by its income tax law, S. L. of Colo. 1927, Ch. 175, Sec. 2, e, (1)) to tax and is taxing the bank, measured by its net income (see paragraph 7, R. 8, and sub-paragraph (5), R. 10-11), and that its vaults and safe-deposit boxes, as*

fixtures in its banking house, are subject to an ad valorem tax and are so taxed as real estate (see paragraph 6, R. 7). If the service tax is a valid property tax measured by income, as in *Alvard v. Johnson,* then the bank will be taxed three times on the one thing. But R. S. Sec. 5219 prohibits state taxation of national banks' real property, except as other real property is taxed.

As we consider this cause, it is not one in which this court is bound by the state court's construction of the Service Tax Act to the effect that the user of the bank's services is the taxpayer, if it made such a construction. Because the act also provides that all services are exempt which the state is prohibited from taxing by the laws or Constitution of the United States, the proper construction of the act for the application of the exemption is not purely local, and the state court cannot, by an erroneous construction, frustrate a valid claim of a federal immunity and foreclose this court from considering it. The correct rule, applicable to this cause, and permitting this court's determination of whether or not the bank is the taxpayer, was stated by this court in *St. Louis S. W. R. Co. v. Arkansas,* 235 U. S. 350, 362, 35 S. Ct. 99, 102, as follows:

> "But when the question is whether a tax imposed by a state deprives a party of rights secured by the Federal Constitution, the decision is not dependent upon the form in which the taxing scheme is cast, nor upon the characterization of that scheme as adopted by the state court. *We must regard the substance, rather than the form, and the controlling test is to be found in the operation and effect of the law as applied and enforced by the state.*"

The foregoing was cited and again stated in substance in *St. Louis, etc., Cotton Co. v. Arkansas,* 260 U. S. 346, 348; 43 S. Ct. 125; and these two cases were cited with approval on this point in *Federal Land Bank v. Crosland,* 261 U. S. 374; 43 S. Ct. 385 (see appellant's brief, page 33),

which in turn was followed and cited with approval in *Pittman, Clerk, v. H. O. L. C.*, 60 S. Ct. 15, decided at this court term (see appellant's brief, page 23).

In our opinion, however, the Colorado Supreme Court did *not* hold that the bank is *not* the taxpayer. Its decision seems to us to be to the contrary. The Colorado Supreme Court said: "The bank does not carry any of the tax burden unless it refuses to comply with certain terms of the act. To that extent, as applied to the bank *it is a taxpayer*" (R. 25). Upon remand, the district court decreed that, to comply with the terms of the act, *the bank must pay the tax whether or not it collects the amount thereof from its customers.* The Colorado Supreme Court thereafter affirmed that decree. The Treasurer alleged that the bank "refused to collect or remit any of said taxes or in any manner comply with the said law" (see paragraph VI at R. 3), and the bank admitted that allegation (R. 6). It follows from this that we have the state court's adjudication that the bank *is the taxpayer* and such is "*the effect of the law as applied and enforced by the state.*" We submit that a state may not, upon threat of duress, force a national bank to be a tax collector, and, upon refusal, to be a taxpayer.

3. *Reply to argument that R. S. Sec. 5219 prohibits no more than discriminatory taxation of national bank shares, and that its sole purpose is to prevent discrimination against national banks in their competition with other moneyed capital.*

This is another thought or argument permeating appellee's brief and is an entirely different position from that which he took in the courts below. There he conceded that R. S. Sec. 5219 prohibits all state taxation of national banks, except as in the section provided (see appellant's brief, page 15). The Colorado Supreme Court held and said:

"It heretofore has been determined that a state can only tax a national bank with the consent of Congress *and not otherwise.* First National Bank v. Anderson, 269 U. S. 341; 46 Sup. Ct. 135, 70 L. Ed. 295, and numerous other authorities. *Section 5219, supra, furnishes the exclusive authority governing state taxation as to national banks.* Bank of California v. Richardson, 248 U. S. 476, 39 Sup. Ct. 165, 63 L. Ed. 372." (R. 20-21.)

Now, however, the appellee attempts to contend that R. S. Sec. 5219 should be construed as prohibiting only discriminatory taxation of national bank shares, and not other state taxation of a national bank, its business or its property. To do so, he quotes, from *First National Bank v. Anderson,* 269 U. S. 341; 46 S. Ct. 135, that part of the opinion relating to the discrimination involved in that particular case, and infers that the prohibition of R. S. Sec. 5219 is thus limited to discrimination only. But the court in that case did not intend to, and did not, so limit the prohibition. This is clearly shown by that portion of the opinion, not quoted by the appellee, appearing at page 347, reading as follows:

"National banks are not merely private moneyed institutions, but agencies of the United States created under its laws to promote its fiscal policies; and hence *the banks, their property, and their shares cannot be taxed under state authority, except as Congress consents, and then only in conformity with the restrictions attached to its consent.* Des Moines National Bank v. Fairweather, 263 U. S. 103, 106, 44 S. Ct. 23, 68 L. Ed. 191, and cases cited. *The early legislation respecting these banks contained a restricted consent, which afterwards became Section 5219 of the Revised Statutes.*"

That R. S. Sec. 5219 should be construed as prohibiting state taxation of national banks, *their property, and*

their business, as well as their shares, is founded upon numerous decisions of this court commencing with *McCulloch v. Maryland*, 4 Wheat. 316, and upon the recognition by Congress, by the legislatures of states, by state administrative regulations, and by state court decisions, of the principle announced in the federal cases over a period of 121 years. An example of state court recognition is that part of the Colorado Supreme Court's opinion quoted above, an example of recognition by state administrative regulation is Section 10 in this matter, quoted at R. 2, and an example of a state legislature's recognition is the Colorado income tax law stated and quoted, in part, in sub-paragraph (5) at R. 10-11.

McCulloch v. Maryland first announced that states were prohibited from taxing banks (including their property, and business), created by Congress under governmental powers, and that permission to so tax must come from Congress. Acquiescing in that and in a long line of similar and subsequent decisions, Congress has, from time to time, extended permission until the full measure of its permission is now embodied in R. S. Sec. 5219 as amended. Thus the section has come to be construed, as stated by the Colorado Supreme Court, supra, as furnishing "the *exclusive* authority governing state taxation," and, being *exclusive*, the section is also construed as *prohibiting* all forms and methods of state taxation not so expressly authorized.

If this be not so, then new forms and methods of state taxation never dreamed of by state legislators or by Congress are subject to state adoption; and the control exercised by the government over national banks through various governmental departments and agencies, such as the Comptroller of the Currency and the Federal Reserve System, will soon be materially weakened unless new federal legislation be adopted, which for many years has been considered wholly unnecessary. Any variation of, or departure from, a principle so long accepted by Congress

and so firmly imbedded in the laws of the nation should come from Congress. It can easily permit state taxation of national banks, their business and property, in new forms and manner, whenever desirable. We respectfully submit that, in this, Congress, and not the courts, should lead the way.

Appellee cites no authorities to sustain his attempt, first made in this court, to disturb this ancient principle of national banking law. We adhere to the position taken in the opening brief of the appellant that this is a case involving a *congressionally recognized immunity,* as distinguished from a case in which the immunity may or may not be *implied* by a court.

4. *Reply to argument that the safe-deposit business is not a national banking function.*

On this feature of appellee's argument he has no supporting authorities, whatever, other than the decision of the court below, and, therefore, contends that, because a national bank is not *required* to conduct a safe-deposit business, or to render that particular service, it is not a banking function.

The Banking Act does not purport, and has never been construed, to "list" or enumerate all of the banking powers thereby conferred upon national banks; nor are the banking powers conferred limited to those particularly mention in R. S. Sec. 5136, as amended, U. S. C. A., Title 12, Sec. 24 (see *Carlisle, etc., Bank v. Graham,* 100 U. S. 699). Instead, the section provides that a national bank shall have the power "to exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the *business of banking.*" What may be the "business of banking" is left to the courts for determination in the light of what is generally understood thereby and of the common law. So, it is that all of the courts, with the exception

only of the Colorado Supreme Court in this case, have held and said that the safe-deposit business was the first, and at first the only, function of banking, and, therefore, when Congress authorized national banks to do a banking business, it authorized them to conduct the safe-deposit business as a banking function.

If, within the discretion delegated by Congress to a national bank's board of directors and duly authorized officers, a national bank does any of those things which are within the broad general definition of the business of banking, then the powers to do those things are included in the powers necessary to carry on the business of banking. They are not rendered unnecessary, within the meaning of the act, as argued by the appellee, because a bank is not *required* to do them.

The exercise of all of the powers granted by Congress is, in each instance, permissive and not mandatory. A national bank may, but need not, as banking functions, do a trust business, have a savings account department, act as escrow agent, make collections, accept special deposits, conduct a safe-deposit department, and a number of other things, none of which are specifically mentioned or listed in R. S. Sec. 5136. But when any national bank does any of these things, because its board of directors or officers deem it advisable for the benefit of the bank, to meet competition, or for any other reason, then the bank is exercising a congressionally granted power "*necessary to carry on the banking business.*"

Further recognition of a national bank's ownership and operation of vaults and safe-deposit boxes and fixtures is the requirement that a national bank, in certain instances, must procure the approval of the Comptroller of the Currency as to the investments made in bank premises. In this case, it is admitted in the pleadings that the bank owns its bank building, and that its vaults, safe-deposit boxes and fixtures are part thereof, in all of

which it has a large investment. (See U. S. C. A., Title 12, Sec. 371 d; Act of Dec. 23, 1913, c. 6, Sec. 24 A; as amended June 16, 1933, c. 89, Sec. 14, 48 Stat. 184; as amended August 23, 1935, c. 614, Sec. 203 (a), 49 Stat. 704.)

Considering the historical aspects of this part of banking and the former opinions of this court upon this subject, as well as the soundly reasoned and logical case of *Bank of Calif. v. Portland*, 157 Ore. 203, 69 Pac. (2d) 273, (certiorari denied 302 U. S. 765), which cannot be distinguished from this case, and that there are no decisions or authorities in support of the appellee's contention and of the decision in the court below, we believe that this court should adhere to the doctrine which it has several times announced, and hold that the conduct of a safe-deposit department is a national banking function.

CONCLUSION.

Our efforts, in this brief, have been to reply to the arguments of the appellee on the substantial questions involved in this cause, and to show the fallacies of his contentions.

We trust this will be an aid to the court in considering, and in correctly determining, this cause, the final decision of which we believe should be a reversal of the court below.

Respectfully submitted,

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